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No. 88-302

IN THE

Supreme Court of the United States

OCTOBER TERM, 1988

JAMES A. GORDON, Special Deputy State Insurance Commissioner of Maryland and Receiver,
Petitioner,

versus

UNITED STATES DEPARTMENT OF THE TREASURY; W.E. DOUGLAS, COMMISSIONER, UNITED STATES DEPARTMENT OF THE TREASURY, FISCAL SERVICE,
Respondents.

BRIEF OF AMICUS CURIAE STATE OF MARYLAND, *EX REL.* INSURANCE COMMISSIONER OF THE STATE OF MARYLAND IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

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OCTOBER TERM, 1988

JAMES A. GORDON, Special Deputy State Insurance Commissioner of Maryland and Receiver for Eastern Indemnity Company of Maryland,

Petitioner

v.

UNITED STATES DEPARTMENT OF THE TREASURY, *et al.*

Respondents

BRIEF OF AMICUS CURIAE, STATE OF MARYLAND, *ex rel.* INSURANCE COMMISSIONER OF THE STATE OF MARYLAND IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

INTEREST OF AMICUS CURIAE, THE STATE OF MARYLAND

Amicus Curiae, the State of Maryland, on behalf of the Insurance Commissioner of the State of Maryland ("Insurance Commissioner") urges this Court to issue a writ of certiorari to review the Opinion of the United States Court of Appeals for the Fourth Circuit, 846 F.2d 272 (1988), in order to decide an issue of great public importance.

The ultimate issue to be decided in this action is whether the Federal "super-priority" statute, 31 U.S.C. §3713[1] preempts the ability of the Receiver of Eastern Indemnity Company of Maryland ("EICOM")[2] to apply the insurance laws of Maryland when conducting the company's business. The Federal statute requires payment to the Government of all amounts owed, on a dollar-for-dollar basis, regardless of any preexisting priority system, and places personal liability upon the receiver/liquidator who fails to obey its mandate. Maryland's Insurance Code, on the other hand, sets out a detailed system to pro-rate the claims against the insolvent carrier, with the aim of ensuring at least partial payment of valid claims against an insolvent insurer. *See*, Maryland Code, Ann., Article 48A, §158A, which provides that claims by "policyholders, beneficiaries, and insureds" have priority over "all other claims except for those expenses of administration, wages . . . and taxes." It is important to note that the claims upon which the Government seeks to assert a priority are merely policyholder claims, similar to all other policyholder claims nationwide, arising out of EICOM's business of surety bond underwriting. The Maryland Code pro-

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[1] This statute provides that a claim of the United States "should be paid first" in the case of an insolvent debtor. The statute further provides that "(a) representative of a person. . . paying any part of a debt. . . before paying a claim of the government is liable to the extent of the payment for unpaid claims of the Government." 31 U.S.C. §3713(b).

[2] EICOM is a Maryland domiciled surety company which was placed into receivership, followed by liquidation, by State court order beginning in 1985, pursuant to Maryland Code, Ann., Article 48A, §§132, *et seq.*

vides that tax claims of the Government are paid up front.

The Petitioner, as Receiver and liquidator of EICOM, wishes to ensure at least partial payment to all policyholders or beneficiary claimants. The Federal Government, however, asserts that the super-priority statute gives it the right to push ahead of all other claimants in seeking repayment from EICOM's meager assets. The Receiver claims that the McCarran-Ferguson Act, 15 U.S.C. §1011 *et seq.*,[3] prohibits the Government's attempt to deny all other claimants access to these assets.

In determining whether the Federal statute should be permitted to disrupt the state-mandated priority of payment scheme, the issue has narrowed to the question whether an insurance company receiver, who takes the insurer's "property and business in his own name . . . or in the name of the insurer",[4] is involved in the "business of insurance", so as to be afforded McCarran-Ferguson Act protection.

The Insurance Commissioner of the State of Maryland is the agency official charged in the first instance with conducting the business of troubled insurers in

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[3] The relevant section of this Act states:

(a) The business of insurance and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

(b) No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance. . .

[4] *See*, Maryland Code, Ann., Article 48A, Section 142.

this State.[5] She therefore has a preeminent interest in the outcome of this litigation, as it will affect not only the conduct of this liquidation, but all future liquidations conducted in Maryland.

Indeed, for more than a hundred years, the regulation of the insurance industry has been the exclusive right and responsibility of the several States. The federal role, both by operation of the McCarran-Ferguson Act and by case law, *Paul v. Virginia*, 75 U.S. (8 Wall.) 168, 19 L.Ed. 357 (1869); *Prudential Insurance Co. v. Benjamin*, 328 U.S. 408 (1946) has been abrogated to the States. This is in recognition of the fact that the insurance industry cannot respond to the needs of policyholders if regulated on a national basis, subject to all federal laws. 15 U.S.C. §1011.

Maryland, like all 50 states, extensively regulates the insurance business conducted within its borders. This regulation extends from the creation of an insurance company, through its operational life, to its termination. As a result, the citizens of Maryland look to the Insurance Commissioner to protect their interests at all stages of an insurer's operation, and to ensure that they receive the insurance protection for which they contracted. The Fourth Circuit decision in this case, if allowed to stand, would eviscerate the Maryland Insurance Commissioner's authority to carry out this public service.

The Insurance Commissioner further believes that a ruling by this Court that the Department of the

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[5] *See*, Maryland Code, Ann., Article 48A, Section 145, which provides in part that upon appointment as receiver, the Commissioner shall "immediately proceed to conduct the business of the insurer" §145(5).

Treasury is entitled to avoid the mandates of the McCarran-Ferguson Act will have a detrimental impact not only upon her ability to conduct liquidations, but also upon her overall regulatory authority.

CONSENT OF THE PARTIES

Pursuant to Rules of the Supreme Court, Rule 36.4, Amicus Curiae State of Maryland is not required to obtain written consent of the parties prior to filing a brief *amicus curiae*, in that it is a State, sponsored by its Attorney General.

ARGUMENT

I. THE INTERPRETATION GIVEN TO THE PHRASE "BUSINESS OF INSURANCE" BY THE FOURTH CIRCUIT WILL SEVERELY IMPAIR OR PROHIBIT THE REGULATION OF INSURANCE BY THE INSURANCE COMMISSIONER

The lower court, in a *per curiam* opinion, held that the McCarran-Ferguson Act is inapplicable to the activities of an insurance company receivership. *Gordon v. U.S. Treasury*, 846 F.2d 272 (4th Cir. 1988). This conclusion was based upon the underlying finding that receivership business does not fall within the McCarran-Ferguson definition of the "business of insurance" as set out in *Union Labor Life Insurance Company v. Pireno*, 458 U.S. 119 (1982), involving an interpretation of the antitrust exemption built into the McCarran-Ferguson Act. *See* 15 U.S.C. §1012(b). The effect of this decision upon the overall regulatory authority of the Insurance Commissioner is grave and holds such far-reaching consequences to the citizens of this and all other states as to warrant review by this Court.

The Maryland Insurance Code, contained in Article 48A[6] of the Maryland Code, sets up a highly complex, intricate system by which the Insurance Commissioner may regulate the insurance industry in this State. The Commissioner oversees the creation of Maryland insurers, Md. Code Ann., Corporations and Associations, Section 6-501, *et seq.*; the financial viability of these companies, §§47-50; the entrance of unauthorized insurers into the Maryland market, §§201-211A; the manner in which companies set rates, §242; the policies they use, §242(d); the risks they choose to underwrite, §234A; and how they may cancel existing risks §240AA, §234B, §240A. The Commissioner is vested with the power to ensure that valid claims are paid on a timely basis. The Commissioner regulates the manner of advertising and solicitation used by insurers, §§212, 217-219, 221; the names a company may use, §234; and myriad other functions, with the sole aim of protecting the insurance-buying public.

An unthinking application of the *Pireno* test in all circumstances would destroy not only the Commissioner's power to ensure that policyholders receive claims payment in a liquidation, but could potentially affect all aspects of her regulatory authority which are of any consequence. The lower court reasoned that, for an activity to be the "business of insurance", it must directly involve the transfer or spreading of risk, and the contractual relationship between an insurer and its insured. This, in effect, limits the scope of the "business of insurance" to the narrow param-

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[6] Unless otherwise specified, all references to the Maryland Code hereinafter shall be to Article 48A.

eters of the "business of contracting." It overlooks the fact that crucial regulatory activities, such as the review and approval of policy forms, have no direct effect upon the *actual* transfer or spread of risk among discrete individuals or the contractual relationship between the insurer and insured. Rather, this is a function involving only the Insurance Commissioner and the insurer. Similarly, Maryland's "Unfair Trade Practices Act" governs the payment of claims, false and deceptive advertising, policy cancellations, nonrenewal procedures, and coerced sales, among other things.

Under the lower court's analysis these consumer protections are not a part of "the business of insurance" because the actual "transfer" of risk occurred at the time of contracting. Yet, pursuant to this rationale, the federal government would be able to preempt the Commissioner's regulatory authority at any time. This is precisely the situation which existed in *Federal Trade Commission v. National Casualty Company*, 357 U.S. 560, where federal authorities attempted to step into various insurance commissioners' shoes, and regulate insurance company advertising. This Court refused to permit this federal intrusion, reasoning that regulatory responsibility had been delegated to the States pursuant to the McCarran-Ferguson Act, and that the States were best equipped to carry out this function.

The Insurance Commissioner does not believe the Government intends to argue that she loses her sovereign authority to regulate the insurance industry and its practices once an individual insurance contract has been signed. Yet, by limiting the definition of the "business of insurance" to only those discrete acts *by*

an insurer which actually transfer or spread risk, the Government has placed the entire regulatory structure of the insurance industry in jeopardy. Only this Court can resolve the ambiguity resulting from the lower court's decision.

The Commissioner's authority to take action in the event a company falls into financial difficulties is jeopardized by the Court of Appeals' decision. By removing the liquidation process from the aegis of McCarran-Ferguson protection, the lower court has drawn an artificial line through the insurance regulatory process, leading to untenable and illogical results which only review by this Court can correct.

Both the Government and the lower court have taken a dangerously myopic view of the liquidation process. It is neither logical, nor practical, to view liquidation in a vacuum. Rather, liquidation is merely the continuation, albeit to termination, of an ongoing business, and is merely the final stage in the lifecycle of an insurance company. The Maryland Insurance Code recognizes that this stage necessarily involves the continuation of the "business of insurance." When an order of rehabilitation is issued, pursuant to §141, the order "shall direct the Commissioner forthwith to take possession of the property of the insurer *and to conduct the business thereof*. . . ." (emphasis supplied). Liquidation is merely the next step. It is logically inconsistent to assert that a company under the control of the Commissioner during rehabilitation is afforded McCarran-Ferguson protection, but that a company in the process of concluding its affairs and paying policyholder claims is not. Yet, the claim that the "business of insurance" does not en-

compass the adjustment and payment of claims by a company in liquidation draws just this arbitrary line, and effectively removes the Commissioner's ability to protect her citizens at precisely the time it is most important that she do so. When the insurance industry, or any of its members is in financial difficulty, it is imperative that the various insurance commissioners retain their regulatory authority. It is precisely in circumstances such as EICOM's that the potential for policyholder injury is greatest.

The consequences of the Fourth Circuit's interpretation are grave. Insurance companies frequently operate in many states.[7] By defining the rehabilitation/liquidation process as outside the "business of insurance", and hence, outside McCarran-Ferguson protection, the lower court creates insurmountable problems for the conduct of receiverships nationwide. If the Fourth Circuit is correct, and receiverships are not the "business of insurance", the several states are robbed of their ability to protect and preserve assets for the benefit of policyholders, by the potential intrusion of overriding and conflicting federal laws and regulations. Yet, there is no other overall scheme to fill the void and ensure this protection. Congress, in recognition of this fact, has declared that the states must be afforded the preeminent right to conduct insurer insolvencies. *Baldwin-United Corp. v. Garner*, 678 S.W. 2d 754 (Ark. 1984). The reasoning of the *Baldwin-United* court, which is in direct conflict with the lower court's decision here, is particularly relevant. It is also particularly illustrative of the unten-

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[7] In Maryland, for example, as of December 31, 1987, 1,291 companies were licensed to do business. Of these, only 56 are domiciled in this State.

able ramifications which would result should the lower court's decision be left unreviewed. In *Baldwin-United*, the parent company of three insolvent Arkansas insurers brought suit in federal court to set aside the rehabilitation plans created for those insurers by the State-run receivership. The Court refused, reasoning that insurance company liquidation intimately involves the relationship between the insurer and its insureds and is, therefore, the "business of insurance" intended to be protected by McCarran-Ferguson:

> The Plan of Rehabilitation protects over 300,000 policyholders throughout the United States by attempting to provide the Arkansas insurance companies with assets at least sufficient to support the full amount of the accumulated value of the annuities.

Baldwin-United v. Garne 678 S.W.2d at 758. As a result, the assets of the insurers were not within reach of the parent corporation, and were available to the State for the benefit of policyholders.

The Arkansas court recognized that the activities of a receiver, including payment of claims and gathering assets with which to pay the claims, is at the very heart of the relationship between a policyholder and its insurer, and is an integral part of the regulatory scheme preserved to the states by McCarran-Ferguson. *See, also, Washburn v. Corcoran*, 643 F. Supp. 554 (SDNY 1986); *Idaho v. IRS*, 662 F. Supp. 60 (D. Idaho 1987), *reversed and remanded*, No. 87-4057 ___F.2d ___(9th Cir). Removing McCarran-Ferguson protection would open the door to actions such as the one contemplated in *Baldwin-United*. Without

clarification by this Court, the scope of the Commissioner's power to fulfill the contractual obligations of an insolvent insurer is in serious doubt.

II. THE INTERPRETATION GIVEN TO THE PHRASE "BUSINESS OF INSURANCE" BY THE FOURTH CIRCUIT IS IN DIRECT CONFLICT WITH PRIOR INTERPRETATIONS BY THIS COURT

In concluding that the settlement and payment of claims by EICOM's liquidator is not the "business of insurance", the District Court and, by adoption, the Court of Appeals, applied a three prong "test" set out by this Court in *Union Labor Life Insurance Company v. Pireno*, 458 U.S. 119 (1982). In doing so, the lower court ignored the fact that the *Pireno* Court was construing the "business of insurance" provision in the context of its narrow antitrust exception. The court failed entirely to address and reconcile *Pireno* with this Court's earlier decision in *Securities and Exchange Commission v. National Securities, Inc.*, 393 U.S. 453 (1969). This misinterpretation will have grave consequences upon insurance commissioners' ability to regulate the insurance industry in their various states. Only review by this Court can resolve this conflict.

The *Pireno* case, in the antitrust context, held that three questions must be answered in the affirmative in order for certain activities to constitute the "business of insurance":

> 1. Does the activity in question relate to the 'spreading and underwriting of a policyholder's risk'? 458 U.S. at 127.
>
> 2. Does the activity in question relate to the contract between the insurer and the insured? 458 U.S. at 128.

> 3. Is the activity in question limited to entities within the insurance industry? 458 U.S. at 129.

In blindly applying these three criteria outside the context of antitrust actions, the lower courts ignored, and thereby nullified, the effect of this Court's reasoning in *National Securities* (involving the SEC's attempt to regulate the merger of two insurers). In that case the Court concluded that the relationship between the insurers and their shareholders was not the "business of insurance," and hence not subject to McCarran-Ferguson protection. The Court reasoned that the relationship of primary importance in the regulatory scheme is the relationship between the insurer and insured. Statutes whose purpose it is to regulate this relationship "directly or indirectly" are preserved from federal intervention by the operation of the McCarran-Ferguson Act. In this way, Congress ensured continued state sovereignty in regulating the insurance industry, and activities which have no nexus to insurance may be regulated by the appropriate entity, federal or state. The Insurance Commissioner believes there is nothing more intimately connected to the relationship between an insurer and insured than the orderly and fair payment of claims.

In holding that the "business of insurance" ceases once a contract of insurance has been signed the lower court also ignored the earlier case of *Federal Trade Commission v. National Casualty Company*, 357 U.S. 560 (1958), which held that advertising by insurance companies is properly left to state regulation, pursuant to McCarran-Ferguson.

If this Court fails to clarify the scope of the phrase "business of insurance", serious questions will arise

concerning the proper interpretation to be afforded to both the *SEC v. National Securities, supra* and *FTC v. National Casualty, supra* decisions.

Indeed, the lower court's decision calls into question the very language of the McCarran-Ferguson Act itself. The lower court definition of the phrase "business of insurance" renders not only the prior decisions of this Court meaningless, but also the language of Section 1014 of the Act.[8] An interpretation of a statute which renders its plain language meaningless or absurd is an incorrect interpretation. *Mountain States Telephone and Telegraph Company v. Pueblo of Santa Ana*, 105 S.Ct. 2586, 2594 (1985); *Colautti v. Franklin*, 99 S.Ct. 675, 684 (1979). Yet neither the Government nor the lower court addressed or reconciled the effect of their interpretation of the phrase "business of insurance" upon this Court's prior pronouncements and on the statute itself.

CONCLUSION

The insurance industry is one of the most highly regulated industries in this country. This pervasive scheme of regulation, encompassing the birth, growth and death of insurance companies, has as its underlying purpose the protection of millions of policyholders and beneficiaries nationwide. Congress, through the McCarran-Ferguson Act, placed the responsibility

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[8]This section states: "Nothing contained in this chapter shall be construed to affect in any manner the application to the business of insurance of the Act of July 5, 1935 . . . known as the National Labor Relations Act, or the Act of June 25, 1938, as amended, known as the Fair Labor Standards Act of 1938 . . ."

to regulate this industry within the jurisdiction of the several states. The lower court decision casts long-reaching shadows over the ability of the states to carry out this mandate, and places in doubt decisions of this Court and of other courts which have faced this question. It is imperative that Maryland's ability to protect its citizens be preserved and that this Court clarify the scope of its sovereign authority to do so. For these and the foregoing reasons, the State of Maryland as *amicus curiae* respectfully prays that the Petition for a Writ of Certiorari be granted.

Respectfully submitted,

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